United States Court of Appeals

for the Second Circuit

BRIEF FOR APPELLEE

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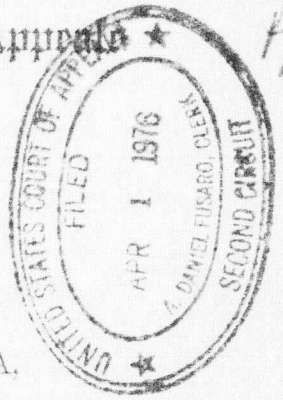

In re:

LOIS ADLMAN,

BANKRUPT,

BANK OF PENNSYLVANIA,

Plaintiff-Appellee,

—against—

LOIS ADLMAN,

Defendant-Appellant.

On Appeal from an Order of the United States District Court for the Eastern District of New York

BRIEF OF PLAINTIFF-APPELLEE

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BRIEF OF PLAINTIFF-APPELLEE

Statement of Case

This is an appeal from an order of the United States District Court for the Eastern District of New York (Platt, D.J.) which affirmed a judgment of the Bankruptcy Court (Radoyevich, B. J.) denying the defendant a dis-

charge in bankruptcy, pursuant to Section 14c(4) of the Bankruptcy Act.

Judge Radoyevich predicated his decision upon the fact findings supported by the testimony that the bankrupt, Lois Adlman, sold her home to her husband's uncle and aunt and took the proceeds thereof and repaid loans on insurance policies amounting to the sum of $52,653.40 and further, paid premiums on such policies amounting to the sum of $7,663.22. The obvious purpose was to put this money into policies of insurance which are exempt from creditors under the Insurance Law of the State of New York and the Bankruptcy Act.

It was, therefore, the Court's appropriate conclusion that by this conduct, the defendant, Lois Adlman, acted "with intent to hinder, delay and to defraud her creditors." (Finding 32 at page 193 of Appendix). Judge Radoyevich found that the bankrupt was under no obligation to repay the alleged "loans" which are considered advancements and if not repaid, are merely deducted "from the amount payable when the policy, by its provisions, matures." He therefore, appropriately concluded: "The repayment of the loans and the advance payment of premiums was nothing more than a voluntary payment which had for its plain intent the removal of the assets involved from the reach of the bankrupt's creditors." (Appendix p. 199).

The Court took judicial notice of the Petition and Schedules in Bankruptcy verified by Lois Adlman showing total liabilities of $4,091,725.20 and no assets other than the life insurance policies having a face value of $275,000.00 He further found (Finding 33) that Lois Adlman executed guarantees of loans which had been made to her husband on his various real property or business ventures. He made essential findings with respect to the loans made by the plaintiff Bank.

The Court below, therefore, made a finding of law (Conclusion 3), as follows:

> "3. The proof does establish that this defendant did, at a time subsequent to the first day of the twelve months preceding the filing of the petition in bankruptcy, transfer her real property, and repay loans on policies of insurance, with the intent to hinder, delay or defraud her creditors, all as specified in Section 14c(4) of the Bankruptcy Act."

The discharge was, therefore, denied to this bankrupt; the judgment entered by Judge Radoyevich was affirmed by Judge Platt upon appeal to the District Court.

Findings of Fact

The findings of fact demonstrate:

1. That the bankrupt, Lois Adlman, in fact executed loan guarantees on her husband's various real property or business ventures;

2. That she was a limited partner in the Leesport Gardens Company;

3. That prior to bankruptcy, the bankrupt and her husband were experiencing financial difficulties;

4. That in October, 1973, roughly five and one-half months prior to filing her bankruptcy petition, was insolvent;

5. That specifically her assets exceeded her liabilities by $4,091,725.20;

6. That in October, 1973, the bankrupt entered into a scheme whereby her residence in Sands Point was conveyed to her husband's aunt and uncle, but at the same time the bankrupt and her husband continued and still continue to occupy the said residence under a lease from the aunt and uncle;

7. That the consideration for the sale of the house included the assumption of a mortgage and $60,000.00 cash;

8. That also in October, 1973, the bankrupt systematically by a series of checks drawn on her banks, deposited $60,316.62 into insurance policies which are exempt from creditors;

9. That the payment on insurance premiums were made in advance of their due dates.

The facts obviously indicate a scheme to isolate both the house and cash assets from creditors, including the appellee, Bank of Pennsylvania. It is highly inconsistent for the bankrupt to testify on the one hand that she and her husband were short on expense money to run the house, and then to testify that upon receiving cash from the sale of the house, to place said cash in exempt insurance policies. This is all coupled with the fact that there is an initial conveyance of the residence to relatives, which is suspect. It seems in fact, that the bankrupt and her husband were in the same position after the above transactions, as previously. They were residing in their home, were still insolvent; only they had now removed both their home and cash in excess of $60,000.00 from creditors.

The conflicts in testimony and factual inferences obviously show an actual intent to hinder, delay or defraud creditors. Both the resolution of conflicting testimony and the drawing of factual inferences from circumstantial evidence, are protected by the clearly erroneous rule. *In re Hygrade Envelope Corp.*, 366 F. 2d 584 (CA 2 NY 1966).

Questions Presented

1. Whether there was substantial evidence and findings of fact upon which the Bankruptcy Court could base its decision denying discharge?

2. Whether the repayment of loans and the prepayment of premiums on policies of life insurance, which are exempt under the law of New York, five and one-half months prior to the filing of a petition in bankruptcy, from sums realized by the bankrupt upon the sale of her home, taken together with all the facts and circumstances surrounding the transaction, constitutes a transfer of property with intent to hinder, delay or defraud creditors under Section 14c(4) of the Bankruptcy Act?

Appellee answers both questions in the affirmative.

3. Were the findings of fact made by Judge Radoyevich as affirmed by Judge Platt "clearly erroneous"?

It is respectfully submitted that the findings were predicated upon and are amply supported by the testimony at which time the Bankruptcy Judge had the opportunity to observe the demeanor of the witnesses and there is no basis for the contention that these fact findings were "clearly erroneous".

POINT I

Findings of fact of the Bankruptcy Judge and the District Court should not be set aside in the absence of a showing that they are clearly erroneous.

Rule 52(a) of the Federal Rules of Civil Procedure, regarding actions tried upon the facts without a jury, states that:

> "Findings of Fact shall not be set aside unless clearly, erroneous, and due regard shall be given the opportunity of the trial court to judge the credibility of the witnesses."

The "clearly erroneous" standard of review by the Court of Appeals is almost too well established for citation. However, it has been enunciated in the U. S. Supreme Court, *McAllister* v. *United States,* 348 U. S. 19 (1954).

It is certainly the rule in the Second Circuit. In the case of *Simon* v. *Agar,* 299 F. 2d 853 (2nd Cir. 1962), the Court stated the following:

> "It is too well settled to require the citation of authorities that where an appeal brings up for review concurrent findings of fact by the referee and the district court, they can be set aside only if 'clearly erroneous' "
>
> * * *
>
> "Particularly is this true where, as in this case the findings involve questions of credibility of witnesses who testified before the referee"
>
> * * *
>
> "Appellant has not carried his burden of convincing us that both essential findings are clearly erroneous."

It is submitted by appellee, Bank of Pennsylvania, that the concurrent findings of both the Referee and District Court, were correct in all regards, and that they are supported by substantial evidence and findings of fact on the record. There is no showing that the Referee's findings of fact were "clearly erroneous".

The standard which must be met by appellant to prove that the findings of fact were "clearly erroneous", is a

stringent one. To be convinced, the Court must be left with the definite and firm conviction that a mistake has been committed. *Seligson* v. *Roth,* 402 F. 2d 883; *Clancy* v. *First National Bank,* 408 F. 2d 899; *Eureka-Carlisle Co.* v. *Rottman,* 398 F. 2d 1015; *Goss* v. *Fidelity & Deposit Co.,* 302 F. 2d 338. The Bankruptcy Court's findings must be upheld if they are supported by substantial evidence *McDowell* v. *John Deere Industrial Equipment Co.,* 461 F. 2d 48.

The trial of this action encompassed two days of testimony, in which the bankrupt among others, was given the opportunity to testify at length regarding the various transactions involved. The Bankruptcy Judge was in the best position to listen to the testimony, take evidence, and draw inferences therefrom. Furthermore, he was in an excellent position to observe the demeanor of the bankrupt and other witnesses, and was able to determine their credibility. All of these factors must be considered in reviewing the Bankruptcy Court's findings of fact.

Now the bankrupt appellant would have this Court on appeal overturn the decisions of both the District Court and Bankruptcy Judge, in total disregard of the Judge's opportunity to judge the credibility of the witnesses. Appellant is grossly in error in taking that approach. On issues such as intent to deceive, or intent to hinder, delay or defraud creditors, where the bankrupt's credibility is an important factor, the Bankruptcy Court's findings should be accorded great weight, since the Judge had the opportunity to hear and observe the bankrupt. F.R.C.P. 52(a); see also: *In Re Ostrer,* 393 F. 2d 646 (2nd Cir. 1968).

A reviewing Court is reluctant to substitute its judgment for that of the Referee who has observed the witness and heard the testimony. *Elliott* v. *Herrera,* 401 F.

2d 174 (9th Cir. 1968). The Referee's determination should be given special weight when the credibility of witnesses is at issue. *In re Mimshell Fabrics, Ltd.,* 491 F. 2d 21 (2nd Cir. 1974).

Furthermore, it is the bankrupt appellant, Lois Adlman, who has the burden of proving that the findings of fact are clearly erroneous. *Seaton* v. *Sills,* 403 F. 2d 710 (5th Cir. 1968). The findings of the District Court are presumptively correct. *Shearman* v. *Missouri Pacific R. Co.,* 250 F. 2d 191 (8th Cir. 1957). Findings come to the Court of Appeals clothed with a presumption of correctness. *In re Souder,* 449 F. 2d 284 (5th Cir. 1971). This is further supported by the proposition as seen in the *Simon* v. *Agar* case, *supra,* that *concurrent* findings of fact by the Referee and District Court, will ordinarily be accepted on appeal.

The overwhelming conclusion is that the findings of the lower Courts must be upheld. It is difficult to see how the Court can be left with any other conviction but that there was a conveyance of property with intent to hinder, delay, or defraud creditors, as supported by the facts.

The facts obviously indicate a scheme to isolate both the house and cash assets from creditors, including appellee, Bank of Pennsylvania, which has been fully discussed in the Findings of Fact, *supra.*

The conflict in testimony and factual inferences, obviously show an actual intent to hinder, delay or defraud creditors. Both the resolution of conflicting testimony and the drawing of factual inferences from circumstantial evidence, are protected by the clearly erroneous rule. *In re Hygrade Envelope Corp.,* 366 F. 2d 584 (2nd Cir. 1966).

The brief submitted by the appellant refers to inferences. In the instant case, we are dealing with factual

testimony and the credibility of the witnesses, as well as the conflicting testimony. It was appropriate for the Bankruptcy Judge to conclude that it was a scheme or intent to defraud the creditors.

POINT II

The placement of non-exempt funds into exempt insurance policies, in light of all the facts and circumstances of this case, indicates actual intent to hinder, delay or defraud the creditors.

There is substantial evidence indicating that the transfer of the bankrupt appellant's funds into exempt insurance policies was fraudulent as to the creditor appellee, Bank of Pennsylvania. It is submitted that in light of all the facts and circumstances, the evidence supports the Judge's conclusion that there was an actual intent to hinder, delay or defraud creditors.

It is conceded that the Bank must prove actual intent to defraud as opposed to constructive intent. However, through the time honored legal devices of inferences and presumptions, the Courts are able to transcend the problem of the search for proof of actual intent. (Cowans, Bankruptcy Law & Practice § 224). Actual intent to hinder, delay or defraud creditors may be proved by circumstantial evidence. *In Re Freudman,* 362 F. Supp. 429 (DCNY 1973); See also: Collier on Bankruptcy, ¶14.47n2, ¶3.105. The Court is permitted to make inferences from the facts and circumstances of the case. *In Re Kehler,* 159 F. 55 (CCA 2d Cir.); Collier *supra* ¶3.107.

The facts as hereinabove set forth, overwhelmingly show either directly or by inference, that the transfer of funds to exempt propery was fraudulent.

Among the factors to be considered are the fact that bankrupt was insolvent both when she made the transfer, as well as at the time of bankruptcy.

Also to be considered is the fact that the cash was received from the sale of the bankrupt's house to her husband's aunt and uncle, with a leaseback of the house to the bankrupt and her husband. The sale of the house was on October 12, 1973. On that very day and within eight days thereof, the bankrupt systematically placed slightly in excess of $60,000.00 into insurance policies. The cash received from the sale of the house was $60,000.00. The inference to be drawn is almost too obvious for further discussion.

The Honorable Bankruptcy Judge Radoyevich rightfully held that here the bankrupt was under no obligation to repay the alleged "loans" on the policies of life insurance. Such "loans" are considered advancements of the sums payable under the policy and if not repaid, are merely deducted from the amount payable when the policy, by its provisions, matures. *U.S.* v. *Sullivan,* 333 F. 2d 100, 112, 113.

Here, we have not just a simple case where a debtor places funds into exempt properties. Thus, the cases cited by bankrupt, *Love* v. *Menick,* 341 F. 2d 680, and *Schwartz* v. *Selden,* 153 F. 2d 334, are inapplicable to the facts at bar. As a matter of fact, there was evidence of a systematic scheme and fraudulent purpose to defraud creditors. Thus, the bald statement on page 14 of appellant's brief to the effect that "The sole basis for the denial of the discharge was the fact that the Bankrupt converted non-exempt property into exempt property", is simply not an accurate statement of the holding of the Bankruptcy Court's decision.

The rights of exemption on insurance policies depends upon State law. *Cowans, supra* ¶20. Thus, New York law applies on this subject. Judge Radoyevich was correct in stating that Section 166 of the Insurance Law creates an exemption for insurance policies. He was further correct in stating that said section also contains an exception which denies exempt status to "the amount of premium or other consideration paid with actual intent to defraud creditors". Thus, in New York, there is no absolution exemption for insurance policies in light of the exception. This case is governed by such decisions as *In re Hirsh,* 4 F. Supp. 708 (DC NY) and *Baxter House, Inc.* v. *Rosen,* 27 A. D. 2d 258, 278 N. Y. S. 2d 442 (1967). The *Baxter* case held that the mere payment of premiums by an insured debtor who was insolvent or rendered insolvent thereby and who allegedly made such payments with actual intent to delay, hinder and defraud his creditors, constituted grounds for recovery by creditors of the amount of such premiums.

Although the burden of proof in the Trial Court initially rested with the creditor bank, where the natural and inevitable result of the bankrupt's acts was to delay or disappoint creditors, a *prima facie* case was made out and the fraudulent intent was properly presumed. *In re Goumas,* 51 Fed. 126 (DC NY); *In re Hughes,* 183 F. 872 (DC NY), the bankrupt did not rebut this presumption.

The bankrupt appellant takes the position that she was not a sophisticated businessman, but rather a housewife. In fact, throughout bankrupt's brief, there is an attempt to negate the element of intent by claiming she was a housewife. This argument is absolutely without merit, particularly, in this era of emancipation.

The record shows in fact, that the appellant, Mrs. Adlman, was a limited partner in the Leesport Gardens

Company, and that she in fact had signed her name to the continuing guarantee. The relatively sophisticated nature in which she managed the sale of house, and the systematic investment of the proceeds by eight separate checks into insurance policies, should put to rest any notion that this woman was acting only as a housewife. In fact, when testifying on the stand, Mrs. Adlman made a very intelligent witness who had the faculties to know and comprehend the nature and consequences of her acts. Thus, there were certainly issues of credibility involved at the trial level for the Judge's determination.

In *David* v. *Annapolis Banking & Trust Co.*, 209 F. 2d 343 (4th Cir. 1953), a bankrupt wife was not entitled to discharge in carrying out her business affairs, where she had signed a financial statement prepared by her husband, and to her knowledge, was to be used as a basis of credit. That case can be analyzed to the facts at bar.

Certainly, the bankrupt should not be allowed to sell her house to relatives, obtain a lease back, and then place the cash proceeds in insurance policies, knowing all the time that she is insolvent, according to her bankruptcy petition.

CONCLUSION

The Judgment of the Bankruptcy Judge and the Order of the District Court should be affirmed.

Respectfully submitted,

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376—Affidavit of Service by Mail The Reporter Co., Inc., 11 Park Place, New York, N. Y. 10007

New York Supreme Court Appellate Division Department

The United States Court of appeals for the Second Circuit

Adlman

Bankrupt,

bk of Pa

State of New York, County of New York, ss.:

HAROLD DUDASH, being duly sworn deposes and says that he is agent for Crowe, Mccoy, Agoglia & Zweibel the attorney for the above named plaintiffa--e;; appellee herein. That he is over 21 years of age, is not a party to the action and resides at 2346 Holland Avenue, Bronx, N. Y.

That on the 1st day of april, 1976, 1976, he served the within brief of plaintiff-appellwv

upon the attorneys for the parties and at the addresses as specified below

Goldman, Horowitz & Cherno, 390 East Old Country Rd. P.O. VBox 630
Mineola, N.Y. 11501

by depositing two copies
to each of the same securely enclosed in a post-paid wrapper in the Post Office regularly maintained by the United States Government at
90 Church Street, New York, New York
directed to the said attorneys for the parties as listed above at the addresses aforementioned, that being the addresses within the state designated by them for that purpose, or the places where they then kept offices between which places there then was and now is a regular communication by mail.

Sworn to before me, this 1st
April, 1976
day of ....., 1976

Roland W. Johnson

ROLAND W. JOHNSON,
Notary Public, State of New York
No. 4509705
Qualified in Delaware County
Commission Expires March 30, 1977